

**CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM  
STATEMENT OF INVESTMENT POLICY**

**FOR  
TREASURY INFLATION PROTECTED SECURITIES**

**June 15, 2007**

*This policy is effective immediately upon adoption and supersedes all previous Treasury Inflation Protected Securities policies.*

**I. PURPOSE**

This document sets forth the investment policy ("Policy") for the CalPERS Treasury Inflation Protected Securities (TIPS) Fund. The design of this Policy ensures that investors, managers, consultants, or other participants selected by the California Public Employees' Retirement System ("CalPERS") take prudent and careful action while managing the TIPS Fund. Additionally, use of this policy assures sufficient flexibility in controlling investment risks and returns associated with the Treasury Inflation Protected Securities Fund.

**II. STRATEGIC OBJECTIVE**

The CalPERS Treasury Inflation Protected Securities Fund shall be managed to provide investor protection against a decline in asset values due to rises in the Consumer Price Index (CPI).

**III. RESPONSIBILITIES**

A. CalPERS' Investment Staff ("Staff") is responsible for the following:

1. All aspects of portfolio management including monitoring, analyzing, and evaluating performance relative to the appropriate benchmark.
2. Reporting to the Committee quarterly and more if needed about the performance of the TIPS Fund.
3. Monitoring the implementation of, and compliance with, the Policy. Staff shall report concerns, problems, material changes, and all violations of Guidelines and Policies immediately and in writing to the Investment Committee. These reports shall include explanations of the violations and appropriate recommendations for corrective action.

B. The General Pension Investment Consultant (“Consultant”) is responsible for:

1. Monitoring, evaluating and reporting periodically, to the Committee, on the performance of the TIPS Fund relative to the benchmark and Policy.

#### **IV. PERFORMANCE OBJECTIVE AND BENCHMARK**

The benchmark for CalPERS Treasury Inflation Protected Securities Fund is the Lehman Total U.S. TIPS Index.

#### **V. INVESTMENT APPROACHES AND PARAMETERS**

A. Investment Approach

Investors in TIPS seek protection from future inflation and have made a specific asset allocation for this purpose. For this reason, this portfolio shall be principally invested in TIPS much of the time. In general, the portfolio is expected to have a duration that is similar to the duration of the Lehman TIPS Index unless expected returns and economic analysis dictate otherwise. Staff will identify those issues in the universe of TIPS which offer the best returns while maintaining the portfolio duration objective.

B. Specific Risk Parameters

CalPERS shall manage the following major categories of fixed income risk:

1. Benchmark Risk addresses whether the Lehman TIPS Index is the appropriate index for TIPS portfolios.
2. Interest Rate Risk is the price volatility produced by changes in the overall level of interest rates as measured by volatility adjusted duration. Duration shall be maintained within +/-10% of benchmark duration.
3. Real Return Risk is the price volatility produced by changes in market inflation expectations. This risk will be monitored and managed through economic analysis that, at a minimum, looks at volatility, expected inflation, and implied inflation.
4. Yield Curve Risk is the price changes induced by changing slope of the yield curve. Yield curve risk can be managed in a controlled and disciplined way by monitoring key rate durations and principal component analysis.

5. Sector Risk is the risk of holding sectors proportionally different than the index.

Sector Ranges: The following ranges by which actual allocations can fluctuate from the benchmark sector weightings:

| <u>Sector</u>       | <u>Index</u> | <u>Sector Ranges</u> |
|---------------------|--------------|----------------------|
| TIPS                | 100%         | 80-100%              |
| Nominal US Treasury | 0            | 0-15                 |
| <u>STIF</u>         | <u>0</u>     | <u>0-5</u>           |
| Total               | 100%         | NA                   |

#### C. Authorized Securities

1. U.S. Treasury Inflation Protected Securities
2. Nominal (not Inflation Protected) U.S. Treasury Securities
3. A Short Term Investment Fund (STIF)

## VI. CALCULATIONS AND COMPUTATIONS

Investors, managers, consultants, and other participants selected by CalPERS shall make all calculations and computations on a market value basis as recorded by CalPERS' Custodian.

## VII. GLOSSARY OF TERMS

Key words used in the policy are defined in CalPERS' Master Glossary of Terms.

Approved by the Policy Subcommittee: June 15, 2007